BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Claim of AMF INCORPORATED *for Refund of Sales and Use Taxes*

Appearances:

For Claimant: Lewis T. Gardiner, Esq.
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Joseph Manarolla
Tax Counsel

MEMORANDUM OPINION

This opinion considers the merits of a claim for refund of sales and use taxes in the amount of $100,000 filed by AMF Incorporated (AMF) on October 31, 1974 as an amended claim for refund.

AMF is a New Jersey corporation which manufactures, sells and leases a diversified line of products.

Pursuant to sales and use tax audit covering period 7/11/66 through 6/30/70, Field Billing Order covering period 7/1/70 through 12/31/71, reaudit dated 1/12/76, and amended Field Billing Order dated 1/12/76, an overpayment of taxes by AMF was disclosed. The overpayment was partially offset by deficiencies in tax also disclosed for the above periods, and reduced by grant of partial refund of tax to AMF by warrant No. 6-845386 dated 8/22/74 in the amount of tax of $30,185.13 plus interest of $14,137.08 and warrant No. 4-699145 dated 5/7/76 in the amount of tax of $15,453.10 plus interest of $6,901.09. (Total tax refunded, $45,638.23.)

Of the balance of the claim for refund amounting to $54,361.77 ($100,000 less $45,638.23), AMF protests $10,352.04, representing that portion of the tax liability asserted in the audit and Field Billing Order set off against the claimed overpayment and which is attributable to the following specific items:

(1) Property taxes on leased equipment paid by the lessees and considered as constituting taxable rental receipts of the lessor.

(2) The imposition of the sales tax on the in-place sale of leased bowling lanes considered as constituting the sale of personal property.

The issues raised by the protested items will be discussed in the order listed above.

(1) *Property taxes on leased equipment paid by the lessee.*

The business activities of AMF include the leasing of bowling equipment to operators of bowling alleys and the leasing of orbitread machines used in tire recapping.

Under the terms of the lease agreements involved here, the lessees are obligated to pay the property taxes assessed against the leased equipment. Generally, the lessee is the assessee and pays the taxes directly to the taxing authority.

AMF has contended that the property taxes assessed against the leased equipment, to the lessee and paid by the lessee, are erroneously and illegally regarded by the Board as constituting taxable rental receipts of the lessor.

The issue raised is not new to the Board. It has been the Board's consistent position that payment by the lessee of the property taxes either directly or indirectly pursuant to the lease agreement constitutes gross receipts from the lease of the property. The issue currently is the subject of litigation (*Machinery Leasing Co.* v. *State Board of Equalization*, Los Angeles Superior Court No. C146797). Until the issue has been finally adjudicated, the Board's position remains unchanged.

(2) *The ''in-place'' sale of leased bowling lanes.*

This item concerns two sales by AMF of leased bowling lanes and related equipment in place located on the premises of (a) Friendly Hills Lanes and (b) Montebello Lanes. The lanes and related equipment (hereinafter bowling alleys) were leased by AMF to lessees who held the underlying lease on the premises. The leased premises upon which bowling alleys were installed were not owned by the purchasers of the bowling alleys and AMF was not the lessor of the premises.

The lease agreements under which the bowling alleys were leased expressly provided that the leased bowling alleys remained personal property, with ownership and title being retained by AMF (lessor). Copy of sample lease submitted for our consideration (copy in file) provides at Article 6(g):

> ''The machines shall at all times remain the sole and exclusive property of AMF (which reserves the right to assign or encumber the machines) and Operator (lessee) shall have no right, title or interest to the machines but only the right to use them under this agreement. . . .''

At the time of the sale of the subject bowling alleys, AMF was the owner of the lanes which remained personal property under the lease, and clearly possessed the right to remove its property from the leased premises. It is relevant that the ''Purchase Order and

Conditional Sales Contract'' entered into for the sale of the bowling alleys (copy in file) expressly provides that the purchaser ''agrees to purchase the equipment described below''. It is also relevant that the described ''equipment'' includes:

> ''16 pr. AMF Magic Circle *Bowling Lanes* with Underlane Ball Returns, Score Projectors attached and *Sub-Foundations*.'' (Emphasis added.)

The contract further provides that:

> ''Title to and ownership of said equipment . . . shall remain in Seller . . . until all of the above payments have been fully made. . . . Said equipment shall *remain chattels and personal property* at all times.'' (Emphasis added.)

The audit has regarded the sales of the bowling alleys as constituting a sale of tangible personal property subject to the tax (Section 6006, Revenue and Taxation Code). The sales price was adjusted by reaudit of 1/12/76 to give effect to the in-place value of the bowling alleys pursuant to Regulation 1596(c).

AMF contends that that portion of the property sold consisting of the ''lanes'' constitute realty the sale of which is not subject to the tax.

For purposes of clarification, the ''lanes'' in question here consist of the hardwood flooring lumber, including the sub-foundations to which it is secured and which extends from the ball return equipment at one end to the pinsetting equipment at the other end, and upon which the bowling ball rolls to the pins. The lanes are constructed of a different type of material than the regular floor of the building and are installed to perform a specific function completely different from that of an ordinary floor. Clearly, the hardwood is not designed for nor intended to be walked upon as a part of the flooring of the building. The lanes do not lose their identity as an accessory to the building.

Bowling alleys have consistently and for a long time been classified by the Board as ''fixtures'' within the meaning of Regulation 1521, which defines fixtures as follows:

> ''Fixtures means and includes items which are accessory to a building or other structure and do not lose their identity as accessories when installed.''

Accordingly, a contract to furnish and install bowling alleys constitutes a construction contract for the improvement to realty. Under such a contract, fixtures are regarded as realty. However, where the lessor of fixtures installs them on leased premises of which he is not the lessor, and retains a right to remove such fixtures, statutorily the fixtures constitute tangible personal property. Section 6016.3 of the Revenue and Taxation Code provides:

> ''Leased fixtures. 'Tangible personal property', for the purposes of this part, includes any leased fixtures if the lessor has the right to remove the fixtures upon breach or termination of the lease, unless the lessor is also the lessor of the realty.''

The statute clearly applies in the instant case.

AMF argues, however, that the Board's classification of bowling lanes as fixtures is erroneous.

The argument is not convincing. The case of *Trabue Pittman Corp.* v. *County of Los Angeles*, 29 Cal.2d 385, a property tax case, cited by AMF in support of its argument was expressly distinguished by the court in *Standard Oil Co.* v. *State Board of Equalization*, 232 Cal.App.2d 91, as not applicable to sales and use tax matters in the classification of property as real or personal. The Board's classification of property for sales and use tax purposes has been judicially approved as has the validity of Regulation 1521. (See *Oliver and Williams Elevator Corp.* v. *State Board of Equalization*, 48 Cal. App. 3d 897; *Honeywell Inc.* v. *State Board of Equalization*, 48 Cal.App.3d 897.)

Furthermore, the leased bowling alleys here involved were by agreement and intent of the parties to remain personal property even though affixed to realty. The agreed classification of the property as personalty also was expressly provided for in the agreement of sale.

> ''Equipment in the nature of trade fixtures, unaffixed by the seller but intended to be affixed by the buyer, or equipment affixed by the seller but to become unaffixed on the sale, is tangible personal property subject to the sales tax; it cannot be conceived that the Legislature intended gross receipts from the sale of the very same property should escape taxation simply because, though removable by the owner as a matter of right, the equipment was sold in place with a present intent that it remain there.'' (*Standard Oil Co.* v. *State Board of Equalization*, 232 Cal.App.2d 91.)

It is concluded that the sales of the bowling alleys constitute sales of tangible personal property subject to the sales tax.

For the reasons expressed in this opinion, the claim for refund, to the extent of $54,361.77, is denied.

Done at Sacramento, California, this 6th day of April 1977.

William M. Bennett, Chairman
George R. Reilly, Member
Richard Nevins, Member
Iris Sankey, Member
Attested by: W. W. Dunlop, Executive Secretary